

Labour's Legacy – Why The Spending Cuts Are Needed

When Labour came to power they changed the rules and reduced financial regulation. They let the banks go wild and house prices soar. Finance companies threw credit cards at people; the offers to borrow money arrived with every post. Personal debt rose to amongst the highest levels in the world.

Typical of financial bubbles everything was fine so long as house prices kept going up and the economy kept expanding. Vince Cable warned that this couldn't happen and that people were vulnerable but his arguments were dismissed by Labour. After all, Gordon Brown said again and again that he had abolished 'Boom and Bust' for ever.

2002 was the last year in which the government balanced its books. The economy was in a credit-fuelled boom and Labour wanted to spend money on public services. They should have got what was needed from taxes on people who could afford it, but instead they opted to borrow the money.

And like a junkie with a credit card having had their first fix they carried on borrowing and borrowing, year after year, spending money the government didn't have, getting the country deeper and deeper into debt.

Then the bubble burst. Someone pointed out that the financial institutions were lending money to pay for assets that weren't worth much, and that the lenders might not get their money back. Panic set in. Banks collapsed.

The gravy train hit the buffers and government finances were wrecked. Taxes stopped arriving but government borrowing increased faster than ever before. Gordon Brown couldn't bring himself to admit that he had failed, that boom had been followed by bust, so he kept on using the credit cards.

People think that the aim of the Coalition Government is to reduce the size of the debt. It's not. Or at least not for many years to come. The new government didn't inherit a huge but static debt, it inherited a debt that was growing and growing and is still doing so at the rate of over £400 million every day.

This year the government will supplement its income by borrowing almost another £150 billion on top, almost equivalent to the cost of everything we will spend on the NHS. Spending will still be way above our income. By 2015, the year of the next election, the size of the debt won't have been reduced at all. In fact it will be very much greater than it is now.

All that the government is trying to do is to stop the debt getting bigger and bigger, but it will be another 5 years before it succeeds in this, by which time the debt will exceed 100% of Britain's GDP and will be amongst the highest in Europe.

It's like trying to bring an oil tanker to a halt at sea. The government isn't trying to turn it around, it's just trying to slow it down and bring it to a halt before it hits the rocks.

But of course, when you borrow money you have to pay for doing so. A major reason for the cuts that have to be made is simply to meet the increase in the cost of annual interest payments. In fact some £30 billion of cuts (that's £30,000 million) have got to be made to meet this extra cost.

Over the 5 year term of this government the plan is to reduce public spending in real terms by just 3%. In 2015 it will in real terms still be nearly 50% greater than it was in 2000. It's true that the cuts in many areas will be much greater than 3%. That's because so much money is going to be used to pay interest on the debt, and because the Government is not going to cut spending at all on the NHS or overseas aid so the burden will fall more heavily on other areas.

Ed Miliband says that the Government is going "too far and too fast". All that needs to be done, he claims, is to halve the size of the 'deficit' over the next four years.

The deficit is not the debt, it's the amount we are spending over and above our annual income.

Labour's plan is to carry on borrowing money, getting the country deeper and deeper into debt. They just plan to borrow a bit less each month than they did when they were in power. They won't say how large they are prepared to let the debt grow. They want to drive the oil tanker forward while claiming that there are no rocks ahead.

Labour got us into this situation by borrowing money at the very time that they should have been reducing the debts. Now they're pretending that there is an easy way out. They are not telling us about the risks of this approach.

The financial markets don't believe that Greece and Ireland are in control of their debts, and they are suspicious of Portugal and Spain. But at present they are content with Britain because they are convinced that the government is doing what is necessary to bring the oil tanker to a halt.

There is no suggestion that they have confidence in the alternative approach being put forward by Labour. The simplistic slogans being voiced by Miliband and Balls pass unchallenged by most ill-informed journalists but the money markets see straight through them.

If the money markets lose confidence in Britain's debt control strategy and start to think that Britain is a bad bet. If that happens, and they push up UK debt repayment interest rates from 3% even a fraction of the way towards the 11% that Greece is having to pay, then we are in deep, deep trouble.

Cuts in government spending are being made now in order to meet the cost of interest payments. Imagine how much greater they will have to be if interest rates soar.